AKADEMISCHES FORUM FÜR AUSSEN-POLITIK - ÖSTERREICH

UNION ACADEMIQUE DES AFFAIRES ETRANGERES - AUTRICHE

UNITED NATIONS YOUTH AND STUDENT ASSOCIATION OF AUSTRIA

ACADEMIC FORUM FOR FOREIGN AFFAIRS - AUSTRIA

EISENSTADT - GRAZ - INNSBRUCK - KLAGENFURT - LINZ - SALZBURG - VIENNA

VIMUN

VIENNA INTERNATIONAL MODEL UNITED NATIONS
02 - 06 August 2015

<u>Preparation Paper/Study Guide:</u>

International Monetary Fund (IMF)

Simulation of an Annual Meeting of the World Bank Group
and the International Monetary Fund

"Beyond the Austerity Versus Growth Debate: Advancing Sustainable Development and Strenghenting Financial Stability"

Content

1. Introduction

1.1 Annual Meeting of the World Bank Group and the International Monetary Fund

The Board of Governors of the World Bank Group (WBG) and the Board of Governors of the International Monetary Fund (IMF) normally meet once a year to discuss the work of their respective institutions. Their meeting is officially known as the "***Annual Meetings of the International Monetary Fund and the World Bank Group***". The first Annual Meetings were held in Washington, D.C., United States in 1946. Since then, itcustomarily takes place there for two consecutive years and in another member country in the third year. In 2015, the meeting will be held in Lima, Peru, 09 -11 October.

The Annual Meetings bring central bankers and ministers of finance and development from the institutions' 188 member countries together. They provide a forum for civil society, private sector executives, and academics to discuss issues of global concern, including the world economic outlook, poverty eradication, economic development, and aid effectiveness.

1.2 Meeting Procedures

A Governor of the World Bank and the IMF chairs the Annual Meetings, with the chairmanship rotating among the membership each year. In our committee at this year's VIMUN, the chairpersons will be represented by the Managing Director of the IMF, Christine Lagarde, and the President of the World Bank, Jim Yong Kim.

During the Annual Meetings of the Boards of Governors of the IMF and the World Bank, Governors consult and present their countries' views on current issues in international economics and finance. The Boards of Governors decide how to address international economic and financial issues and set priorities for the organizations.

2. The IMF and the World Bank

The International Monetary Fund (IMF) and the World Bank are institutions in the United Nations system. They share the same goal of raising living standards in their member countries. Their approaches to this goal are complementary, with the IMF focusing on macroeconomic issues and the World Bank concentrating on long-term economic development and poverty reduction.

2.1.1 International Monetary Fund (IMF)

The IMF promotes international monetary cooperation and provides policy advice and technical assistance to help countries build and maintain strong economies. The IMF also makes loans and helps countries design policy programs to solve balance of payments problems when sufficient financing on affordable terms cannot be obtained to meet net international payments. IMF loans are short and medium term and funded mainly by the pool of quota contributions that its members provide.

2.1.2 World Bank Group (WBG)

The World Bank promotes long-term economic development and poverty reduction by providing technical and financial support to help countries reform particular sectors or implement specific projects—such as building schools and health centers, providing water and electricity, fighting disease, and protecting the environment. World Bank assistance is generally long term and is funded both by member country contributions and through bond issuance.

3. The Austerity versus Growth Debate

Triggered by the Lehman bankruptcy in 2008, the global financial crisis has caused a majorloss of output and income in most economies of the globe. The World Financial and Economic Crisiswas accompanied by various nationalfinancial and bank crises triggering sovereign debt and constitutional crises like we see in Greece. In addition,crises sparked famine and turmoil in poorer and developing countries.

The views within politics and science are diverse as tocauses and possible solutions of the crisis as well as to the crisis's extent and persistence. There are diverse opinions that range from predicting a speedy recovery to many years of stagnation.

In 2012, the Bank for International Settlements declared during the “Board of Governors of the Federal Reserve System 2012 Conference” that debts are not to be solved with more debts and suggested an austerity policy[1]. Olli Rehn, former European Commissioner for Economic and Monetary Affairs and the Euro of the European Commission, urged countries to meet fiscal targets and to cut spending in order to emerge from its debt crises[2].

Voicing a contrary view, the American Nobel Laureate, economist, and Yale-professor Robert Shiller warns against excessive saving and has called on Europe and the United States to boost economy through growth programs[3]. The chief economist at the IMF and professor at MIT Olivier Blanchard also pointed out that forecasters significantly underestimate the increase in unemployment and the decline in domestic demand associated with fiscal consolidation. Government austerity efforts would therefore undermine economic growth[4].

4. Europe between austerity and growth

Fierce debate is growing in Europe over whether austerity or growth offers the best strategy to overcome the continent's sovereign debt crisis. Advocates for austerity claim that cutting spending is vital to making public finances sustainable, build credibility with investors and create conditions for healthy growth that is not based on real estate bubbles or ever more borrowing. Poor growth of Euro-countries is a long-lived structural problem and is not due to recent austerity measures.

Proponents of growth, on the contrary, argue that synchronized austerity across Europe will only aggravate economic contraction, increase unemployment and make it harder for debt-laden countries to reduce their deficits and restore market confidence.

Both sides agree that structural economic reforms to boost potential growth by removing barriers in Europe's single market and making labor laws more flexible can help in the medium term. They differ mostly about the pace of debt reduction.

It’s worth noting the IMF’s recent aggressive stance on debt reduction. In a report on Greece’s economy in mid-July, the IMF threatened to withdraw support for Greece’s bailout if a future deal did not include substantial debt relief. The IMF has also called for as much as EUR 60 billion in aid to Greece and predicting a potential Greek shortfall of as much as EUR 85 billion.[5]

4.1 The European Sovereign Debt Crisis

The European debt crisis, also known as Eurozone crisis, erupted in the wake of the Great Recession and was characterized by an environment of overly high government structural deficits and accelerating debt levels. Since the end of 2009, the European debt crisis has been taking place in several Eurozone member states. Greece, Portugal, Ireland, Spain, and Cyprus were unable to repay or refinance their government debt or to bail out over-indebted banks under their national supervision without the assistance of third parties like the EFSF, the ECB, or the IMF. Portugal, Ireland, and Greece belong to the group of IMF creditors with the highest open loans.
Eurozone states had to be rescued by sovereign bailout programs, which were provided jointly by the International Monetary Fund and the European Commission, with additional support at the technical level from the European Central Bank (the so called “Troika”). Concerns intensified in early 2010 and thereafter, leading European nations to implement a series of financial support measures such as the European Financial Stability Facility (EFSF) and European Stability Mechanism (ESM).

The crisis had significant adverse economic effects and labor market effects for the worst affected countries, with unemployment rates in Greece and Spain reaching 27%, and was blamed for subdued economic growth, not only for the entire Eurozone, but for the entire European Union. As such, it can be argued to have had a major political impact on the ruling governments in 8 out of 19Eurozone countries, contributing to power shifts in Greece, Ireland, Italy, France, Portugal, Spain, Slovenia, Slovakia, and the Netherlands.

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[1] http://www.bis.org/speeches/sp120321.htm
[2] http://www.reuters.com/article/2013/01/11/eu-rehn-imf-idUSL5E9CB4XA20130111
[3] http://www.handelsblatt.com/politik/wirtschaftskrise-oekonom-shiller-warnt-europa-und-die-usa-vor-uebertriebenem-sparen/7436068.html [DE]
[4] http://www.imf.org/external/pubs/ft/wp/2013/wp1301.pdf
[5] http://www.nytimes.com/2015/07/15/business/international/international-monetary-fund-proposed-greek-debt-relief.html?_r=0

4.2 Some country positions

Most of the western world urges the Eurozone to do more to foster growth whereas **Germany** and like-minded statessuch as the **Netherlands**, **Austria**, the **Scandinavians** and the **Baltics** are warning against letting up on austerity. While **France**, **Italy**, **Greece**, and others are pressing for a loosening of fiscal strait-jackets to allow time for economic reforms, Berlin insists on budget austerity as a precondition to healthy growth. Italy has warned against too rigidly following Germany's preferred approach. The president of the **European Central Bank**, Mario Draghi, is pushing for Germany to loosen up and the **IMF** urged Germany to ramp up spending to stimulate the economy.

4.2.1 Germany

Germany has taken a distinctive position in pushing austerity measures,the ESM, and the restructuring of the European institutions and in pursuing a Europe of several speeds. In 2009, the country has established a debt brake in its constitution.This is with regard to the upper limit of the deficit even more severe than the fiscal treaty prescribes: The budget of the Federal may only have a deficit of 0.35 percent from 2016. The budgets of the countries may record no more deficits.The government of German Chancellor Angela Merkel has agreed on budget cuts to bring Germany's deficit within European Union limits of three percent of GDP.German policy makers and voters generally believe that excessive public spending does not help to generate economic growth in the European crisis states who also suffer from high debt levels.

The austerity plan is ambitious combiningdeep spending cuts with revenue-raising measures. The savings include controversial cuts to welfare payments for the long-term unemployed and reductions in parental allowance for families. Merkel tried to head off critics by pointing out that the plan was fair because it included cuts to industry and the public sector.Europe's biggest economy is hoping to set an example of budget discipline for other countries so they in turn will also tighten their belts.

Most recently, Chancellor Merkel got a less-than-unanimous mandate from the German Parliament to pursue a bailout deal with Greece, with half of her own conservative bloc voting against starting talks.[6]

4.2.2 Greece

The Greek government-debt crisis is the most hazardous of all current sovereign-debt crises in Europe. In late 2009, investors developed concerns about Greece's ability to meet debt obligations. This led to a crisis of confidence. Greek citizens' income has declined, the political landscape has changed radically, unemployment has increased, the Greek parliament has passed seven austerity packages between 2010 and 2013, and protests and riots are very frequent.

In 2010, then-Prime Minister George Papandreou formally requested an international bailout for Greece. The European Union, European Central Bank and International Monetary Fund agreed to participate in the bailout. The IMF, Prime Minister Papandreou, and other Eurozone leaders agreed to the first bailout package for EUR 110 billion (USD 143 billion) over 3 years. Greece-wide riots and revolts broke out. In 2011, anti-austerity protests in Thessaloniki took place. Similar incidents occurred in several other Greek cities and Prime Minister Papandreou resigned.

In 2012, already the fifth austerity package was passed by the Greek parliament amid violent protests and the second bailout package was finalized. It brought the total amount of Eurozone and IMF bailouts to EUR 246 billion by 2016, which was 135% of Greece's GDP in 2013. Many buildings in the center of Athens were burned during the riots. In April 2012, a retired pharmacist committed suicide in front of Greece's parliament as an act of protest against austerity. He became a symbol for groups opposing the austerity measures, and violent clashes between police and demonstrators erupted in Athens.

In January 2015,Syriza won a historic victory.Syriza and the Independent Greeks joined to form a new coalition government. Alexis Tsipras was sworn in as the new Prime Minister. Yanis Varoufakis became the new finance minister. In June 2015, Alexis Tsipras announced a referendum on a bailout agreementto be held on 5 July 2015. He also announced a weeklongclosure of Greek banks, while strict capital controls were imposed.Greece thenmissed a payment on an IMF loan and fell into arrears. The Greek bailout referendum resulted in abandoning the proposed austerity measures by the EU.In its aftermath, the key parties met again for negotiations and agreed to a framework for yet another Greek bailout – the third of its kind.

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[6] http://www.nytimes.com/2015/07/18/world/europe/germany-greece-bailout-talks.html

While many, if not most, agree that the Greek debt is unsustainably high, the debate rages on with the Greek Prime Minister Tripras continuing to clash with German Chancellor Merkel over the terms of the deal. The issue of debt relief is an area of particular contention. This and other areas promise to be hotly debated in the near future.[7]

4.2.3 *France*

In 2012, France held a presidential election in which the winner, Socialist François Hollande, had opposed austerity measures, promising to eliminate France's budget deficit by 2017 by canceling recently enacted tax cuts and exemptions for the wealthy, raising the top tax bracket rate to 75% on incomes over one million euros, restoring the retirement age to 60 with a full pension for those who have worked 42 years, restoring 60,000 jobs recently cut from public education, regulating rent increases, and building additional public housing for the poor. The country disagrees over austerity policy led by Germany.

4.2.4 *Italy*

Italy is trying to push the EU towards focusing on growth rather than austerity. Italian Prime Minister Renzi, since coming to power in February 2014, has advocated for policies promoting growth in Europe and scrapping draconian austerity measures. The country’s Economy Minister Padoan warns of being trapped in a sterile debate over austerity.Italy has long sought to shift the policy debate in Europe away from budget rigor and towards measures to boost economic growth and job creation.Comments by Padoan point to a possible confrontation with traditional defenders of budget orthodoxy in the Eurozone such as Germany or Finland.After dipping in and out of recession since 2008 and posting a 0.1 percent fall in gross domestic product in the first quarter of 2014, the Eurozone's third largest economy still has youth unemployment of more than 43%.

After years of restrictive budget policy, with EUR 182 billion (USD 248 billion) of tax hikes and spending cuts over the past three years, Italy has become increasingly impatient with calls for further budget tightening.A combination of moderate debt servicing costs, caused by low interest rates, rigorous public finance policy and structural reform should enable the debt to fall.

4.2.5 *Spain*

Although Spain's debt-to-GDP ratio is still a relatively high 92 percent, it is still incomparable to Greece's 175 percent debt burden. Spaniards have suffered plenty of economic misery the past few years but the country’s recent economic performance seems optimistic. A further growth of the GDP is expected. The return to Spain’s growth is often interpreted as a result of the tough austerity measures, which have helped Madrid to get its fiscal house in order.

However, large anti-austerity marches in Madrid earlier this year in support of Podemos led some to question whether Spain could become the "next Greece". The party sees Greece in the role of the victim. The country's political parties are readying themselves for a general election in December 2015 that could see the young anti-austerity party take a significant step towards power.A poll published in early July in Spain's national newspaper El Pais put Podemos in third place, running close behind the ruling People's Party and socialist-democrats PSOE with 21.5 percent of the vote.[8]

4.2.6 *Finland*

Finnish Financial MinisterStubb has said the northern European country needs to strike a balance between austerity and growth. Due to Finland's weak economy, its government may have to cut spending further over the next few years to stop national debt levels exceeding EU limits. The small Nordic economy, whose strong exports and government finances were once hailed as a model for the Eurozone, is now in its third year of recession. Shrinking revenue and output is bringing it close to the European Union debt ceiling of 60 percent of gross domestic product and the country calls for smart austerity programs.

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[7] http://www.nytimes.com/2015/07/24/world/europe/personalities-clashing-over-how-to-handle-new-greek-bailout.html?&moduleDetail=section-news-1&action=click&contentCollection=International%20Business&region=Footer&module=MoreInSection&version=WhatsNext&contentID=WhatsNext&pgtype=article

[8] http://www.cnbc.com/2015/07/15/spains-podemos-attacks-greek-bailout-deal.html

4.2.7 *United Kingdom*

UK economic performance has been dismal in recent years. Compared with historic trends, GDP per capita was nearly 16% lower in 2014 – a loss of about £4,500 per person. The much-lauded growth rate of 2.7% in 2014 only looks good in light of population growth, poor overall Eurozone performance and a generally stagnant British economy since the 2008-09 global financial crisis.Jobs have held up surprisingly well with almost three quarters of the working age population in jobs, bringing the UK back to pre-crisis levels.

In 2010, the coalition government created the Office for Budget Responsibility (OBR) to make independent fiscal judgements and assess the government's plans.The coalition accelerated austerity already planned by the outgoing Labour government, taking out an additional 1.2% of national income. VAT was increased to 20% in 2011 and an addition £32 billion of spending cuts announced by 2015.In the December 2014 Autumn Statement, the Chancellor laid out his plans through 2019-20. The aim is to have a £21.6 billion surplus on the overall budget achieved through cutting public spending to 35% of GDP.This will come from reducing real spending on public servicesby 14.1%. The other half of public spending is welfare and this is projected to continue rising by 13%. The current plans are continued and severe austerity.

4.2.8 *The Baltics*

All three Baltic states implemented drastic austerity measures to recover from deep recessions triggered by the 2008-09 global financial crisis, paving the way for Eurozone entry and stable economic growth, now around three percent in the region.

During the global financial crisis, the Latvian economy went from boom to bust in the space of nine years. Latvia then received an international bailout in exchange for severe austerity measures and structural reforms. Latvia's economy returned to growth in 2011 and 2012, outpacing the other 27 nations in the EU, while implementing significant austerity measures. Advocates of austerity argue that Latvia represents an empirical example of the benefits of austerity, while critics argue that austerity created unnecessary hardship with the output in 2013 still below the pre-crisis level. The country has been particularly outspoken on the issue of Greek debt relief. In late July, the Latvian President announced publicly, "Greece's debt is so great that everyone understands — it will not pay."[9]Thus, even while seemingly profiting from austerity itself, proponents of Greek debt relief may have found themselves a new ally.

In Lithuania, politicians are also struggling to explain to their electorate why a country that tightened its belt should now pay for one that refuses to do so. Lithuania's president, Dalia Grybauskaitė, has been one of the most outspoken opponents at EU summits of doling out more cash to Greece.For her, the Greek government needs to take responsibility for their actions and implement the difficult measures demanded by its creditors. She regrets that "the new government is not willing to take responsibility and is asking somebody else to pay for [its] irresponsible reactions".[10]Estonia, the Eurozone's smallest member since 2011, approved an initial Greek bailout but has since said 'No' and now insists that all Eurozone members adopt its strict fiscal discipline. The country is one of the leading voices from the Baltics, advocating a tough approach towards Greece that mirrors the tough reforms Estonia itself took to join the euro in 2011. The three Baltic countries have long insisted they are too poor to pay for the mistakes made by wealthier Greece and that it should have stuck to the reforms and austerity measures laid out in its massive EUR 240 billion (USD 273 billion) bailout.

4.2.9 *Slovakia*

The ex-communist nation of 5.4 million people that joined the Eurozone in 2009, has suffered stubbornly high unemployment despite brisk economic growth in recent years. The country shares the Baltic view. While Germany is frequently portrayed as the biggest obstacle to Greece's new leftwing government, Slovakia's hard line is a reminder that Berlin is hardly alone. "If Slovakia managed to carry out reforms then Greece has to be able to do it, too, there is no room for mercy from our side", said Slovakian Prime Minister Robert Fico.The Eurozone's poorer former communist nation, having itself endured painful reforms and austerity programs, is taking a hard line on Greece after its people voted to reject creditors' bailout terms.

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[9] http://www.nytimes.com/2015/07/24/world/europe/personalities-clashing-over-how-to-handle-new-greek-bailout.html?&moduleDetail=section-news-1&action=click&contentCollection=International%20Business&region=Footer&module=MoreInSection&version=WhatsNext&contentID=WhatsNext&pgtype=article

[10] http://www.france24.com/en/20150704-talking-europe-dalia-grybauskaite-president-lithuania-greece-russia-putin-nato

4.2.10 Poland

Before the crisis, annual Polish GDP growth was around 6 percent. While EU GDP contracted by 4.5 percent, Poland was the only country in Europe to see GDP rise by 1.6 percent in 2009. Expectations for growth are up to 3.5 percent in 2015. Unlike many other countries in Europe, the Polish government did not push through harsh austerity measures during the crisis. Instead, it cut taxes and funded public spending through foreign assistance. Several economic reforms had already been pushed through after the fall of communism in the 1990s, what may be a reason for Poland's better performance during the crisis, compared to other EU countries.

RafalTrzaskowski, the Polish minister for European affairs, said that Poland, like other countries in Eastern Europe, would demand tough reforms from Greece. However, Poland supported coming to an understanding with Greece on sensible terms because Athens did not bear sole responsibility for its economic crisis."It is important to remember that someone lent them money without thinking too much about the consequences", he said.[11]

4.2.11 Iceland

The North Atlantic nation, whose spectacular 2008 meltdown came to symbolize the greed and mismanagement of the global financial system, is expected to begin unwinding the bankruptcies of its three main banks and lifting controls on the movement of capital in and out of the island. Iceland has rebounded after the 2008/9 crisis and is now expected to surpass pre-crisis output levels. The country has been one of the top economic performers in Europe over the past several years in terms of economic growth and has one of the lowest unemployment rates. Iceland's strong balance of payments has allowed it to repay all of its Nordic loans earlyas well as much of its IMF loans while maintaining adequate foreign exchange reserves. However, public and external debt ratios are still high, although on a downward sustainable path.[12]

Instead of pumping money into its ailing financial sector, the national parliament of Iceland, the so-called Althing, opted to let three giant banks fail. The Althing also introduced currency controls and pursued a vigorous policy of employment creation, bringing together educational institutions and the private sector with backing from the state. According to the Islandic President Grímsson, those measures, together with sustained investment in green energy and environmentally sustainable development has provided the impetus for an Icelandic economic recovery.[13]

5. Austerity vs Growth debate in other parts of the world

5.1 China

For the last two decades, China's amazing growth has been fueled by exports to the West. However, in recent years, as export growth has slowed, the government has launched major infrastructure programs for roads, railroads, and energy. At the same time, the private sector has supported huge urban real estate developments. The "growth" question in China is where future jobs will come from. Exports are no longer generating new jobs, urban real estate development is slowing, and more infrastructure investment seems ineffective. The hope is that demand from the growing middle classes will pick up the slack.But much of the demand from the growing middle class will be for Western products. And this is the point at which discussions of austerity start.China's growth has become increasingly dependent on investment, a pattern that will be difficult to sustain. Therefore, there is a need to accelerate progress in transforming the economic growth model to be more reliant on consumer demand.[14]

5.2 Japan

Japanese Prime Minister Shinzo Abe's ruling party urged the government to cap spending for the fiscal year from April 2018, countering views within the administration that has stressed growth over austerity to mend public finances. Japan's public debt is more than twice the size of its economy, by far the worst in the

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[11] http://www.nytimes.com/live/greek-debt-crisis-live-updates/little-sympathy-for-greece-in-parts-of-eastern-europe/
[12] http://www.imf.org/external/pubs/ft/survey/so/2015/car031315a.htm
[13] http://www.iese.edu/en/about-iese/news-media/news/2015/february/icelands-experiment-in-doing-things-differently/
[14] http://www.morssglobalfinance.com/austerity-and-growth-perspectives-europe-the-imf-china-and-the-us-2/

developed world.Some government officials, however, are concerned that it would hamper economic growth, at a time when policy is directed toward lifting the economy out of a long phase of deflation.
The government is aiming to cut a primary budget deficit - excluding debt servicing and new bond sales - to 1 percent of GDP in fiscal 2018 from the current fiscal year's 3.3 percent, and bring about a surplus two years later.[15]

5.3 United States of America

Following the recession, President Obama resisted calls from Congress to cut spending and the Federal Reserve lowered the federal funds rate target rapidly to near zero. A series of anti-austerity measures at the federal level, enacted in the first days of the Obama administration, cushioned the effects of the crisis. In an attempt to fix these economic problems, the United States federal government passed a series of costly economic stimulus and bailout packages. Most notably, the American Reinvestment and Recovery Act (ARRA) was passed in February 2009.It included extended and increased unemployment insurance, subsidized health coverage for laid-off workers, increased food stamp and other safety net benefits, payroll tax reduction, support for city and state governments and investment in transportation and infrastructure programs.

The nation's retreat from tax cuts and spending increases to promote the recovery has been a bipartisan affair. Democratic President Barack Obama and Republican House Speaker John Boehner agreed in 2011 to apply the fiscal brakes by negotiating USD 1 trillion in spending cutbacks over 10 years and a process to impose more.

The Obama administration has repeatedly criticized the big European nations, especially Germany, for running austerity programs of deep spending cuts and tax increases that the administration says slow their own growth and undermine the global recovery. However, figures from the Organization for Economic Cooperation and Development (OECD) show that since the 2009 start of the recovery, the administration has allowed U.S. policy to tighten by more than twice as much on average as Germany, France, Italy and the U.K.

5.4 Brazil

The IMF lowered its 2015 forecast for Brazil's economic performance to a 1 percent contraction from the 0.3 percent growth it forecast in January due to tighter fiscal and monetary policies and a drop in investment by state-run oil company Petrobras. According to the International Monetary Fund, the South American country could return to growth in 2016 if it succeeds in boosting investor confidence with its austerity drive. Faced with an imminent recession, President Dilma Rousseff has embarked on an aggressive drive to cut public spending and raise taxes to balance the government's overdrawn accounts. Finance Minister Joaquim Levy mentioned that the belt-tightening is needed to guarantee sustainable growth in the world's No. 7 economy.The elimination of subsidies and cuts to welfare benefits is a politically sensitive task in Brazil, where mass demonstrations were provoked by an unexpected rise in bus fares in 2013.

5.5 Argentina

According to the IMF, growth outlooks for Argentina have been weakening in past years and now look increasingly dim. In spite of relative investor optimism and moderate external indebtedness, macroeconomic imbalances and negative growth rates prevail. For now, the Argentinian government has relied on fiscal expansion, especially through the central bank, to prop up the economy while an ongoing standoff with investors prevents the country from borrowing outside the country. Many of these policies are seen as more damaging than actually helpful, and the IMF expects the elections of October to put a stop to many of the most disruptive measures. As is, Argentina is projected to grow at a negative rate of 0,7% in 2015.[16]

5.6 Venezuela

According to the World Bank, Venezuela achieved high growth rates up until 2013 where a drastic slowdown even resulted in negative growth in 2014 and 2015. Benefiting from decades of high oil prices, 96% of Venezuelan exports are represented by oil; the Venezuelan government has worked aggressively to reduce poverty. After the precipitous fall in oil prices, Venezuela faces significant challenges, especially since the country already experienced fiscal deficits when growth and oil prices were high.[17]

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[15] http://www.cnbc.com/id/102761515
[16] http://www.imf.org/external/pubs/ft/reo/2015/whd/eng/pdf/wreo0415.pdf
[17] http://www.worldbank.org/en/country/venezuela/overview

Finally, a strongly expansive monetary policy has driven inflation to the highest level in the world– a staggering 95%. The IMF has even gone as far as labeling the economic prospects in Venezuela an “economic crisis” and blames high inflation and recession on years of unsustainable macroeconomic expansion and heavy-handed microeconomic intervention.[18]

5.7 Russia

The news about Russia’s economy keeps getting worse. The IMF predicts that the country’s GDP will shrink by 3 percent in 2015. Unemployment is rising, too. Moscow has already spent USD 100 billion fighting the crisis. The Kremlin is adopting a strategy of austerity, including budget and pension cuts. Given that Putin’s rule has been predicated on steadily rising living standards, the Russian government’s response to the crisis risks undermining the foundations of its own legitimacy.

For most of Putin’s time in office, high oil prices have made it possible to avoid tough decisions about distribution. Throughout the 2000s, Russia’s economy was rapidly growing. The ongoing recession, however, will bring distributional questions to the fore.Inflation has crept upwards even as wage growth has slowed, degrading the purchasing power of Russians’ incomes. Unemployment is increasing. The devaluation of the ruble will raise prices for imported goods, forcing Russians to cut back not only on luxuries such as European holidays, but also on basics such as clothes and food, much of which is imported.In response to the crisis, Russia is cutting government spending by 10 percent across the board, except for the military’s rearmament program, which will be maintained at current levels. This will reduce the provision of education, health, and other social programs.

6. Where we stand today

Global growth remains uneven and prospects of a new mediocre persist. Recovery in the United States, United Kingdom, and India gained momentum,while growth elsewhere met or fell short of expectations, including in some large emerging market economies (Brazil, Russia)[19].
Global growth is expected to remain essentially unchanged in 2015, as lower oil prices and a rebound in advanced countries offset a slowdown in emerging markets. Overall, the medium-term global outlook remains weak.

While the financial crisis has caused a credit crunch, with banks deleveraging their balance sheets and the corporate sector cutting costs, austerity, i.e. reduced spending for private and public consumption, has destroyed the incentives for further investment in some regions of the world; in other parts, however, it seemed to be a remedy for recovery, thus the right political decision.

7. Policy Priorities according to the International Monetary Fund

Decisive policies are needed to boost today’s demand, tomorrow’s growth potential, and to build resilience against existing and emerging challenges. Actions are needed to increase the effectiveness of monetary and fiscal accommodation, ensure durable financial stability, pave the way for higher medium-term growth, and instill a new multilateralism to secure a sustainable future.

A durable rebound in activity and employment needs to be supported bygrowth-friendly fiscal policies and frameworks, while placing debt on asustainable path. Where available, fiscal space should be used to boost demand. Stronger fiscal frameworks would support long-term growth and help manage fiscal risks.

Policies should address private sector debt overhang, manage rising corporate leverage, and enhance resilience against global financial market turbulence. Decisively implemented structural reforms are urgently needed to revive business confidence, investment, job-creation, and to lift potential output. This could be an essential complement to demand-boosting efforts.

[18] http://www.imf.org/external/pubs/ft/reo/2015/whd/eng/pdf/wreo0415.pdf

[19] http://www.imf.org/external/np/pp/eng/2015/041315.pdf

8. Potential points to be addressed in the resolution

What may be the right balance between austerity and growth measures in order to advance sustainable development and strengthen financial stability?

What actions can be taken in order to…
… increase the effectiveness of monetary and fiscal accommodation,
… ensure durable financial stability,
… pave the way for higher medium-term growth,
… secure a sustainable development future?

How can fiscal policies provide growth support and bolster fiscal frameworks?
What measures can be taken in order to improve monetary policy effectiveness and strengthen frameworks?
What structural reforms are needed to lift growth potential?
To what extend can multilateralism secure a sustainable future?

9. Further readings

file:///D:/Downloads/austerity_and_growth_2_FINAL.pdf
http://www.economonitor.com/blog/2013/10/austerity-and-growth-dispelling-confusion-with-some-facts/
http://www.reuters.com/article/2014/10/05/us-global-economy-idUSKCN0HU06E20141005
http://www.imf.org/external/pubs/ft/wp/2013/wp1301.pdf
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